High Cost Support

Competition and Cost Control

General Communication Inc.

Rural High Cost Support – Impact of HCLS

- Federal USF covers 100% of ILEC loop costs > 150% ($33.39) of adjusted Nationwide Average ($22.26 in Dec. 2002)
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- Federal USF covers 90% of ILEC loop costs at or above 115% ($25.60) of adjusted Nationwide Average, but below 150%.

- Non-USF unseparated loop recovery capped at $28.94 ($25.60 + $3.34).

Rural High Cost Loop Support

Costs per Working Loop	Interstate % USF (LTS/ICLS)	Intrastate % USF (HCLS)	Total % USF
≤ 150% Nationwide Avg. Loop	25%	75%	100%
115% ≤ x < 150% Nationwide Avg. Loop	25%	65%	90%
< 115% Nationwide Avg. Loop	<$6.50 SLC	0%	<$6.50 SLC

Rural ILEC USF – No Incentive to Reduce Costs

- ≤ 150% of Nationwide Avg. Loop, all carrier loop cost reductions lower *future* USF payments $ for $.
- At or above 115% of Nationwide Avg. Loop, but below 150%, $.90 of $1 of carrier cost reduction lowers *future* USF payments.
- No independent mechanism to scrutinize rural ILEC "costs," so system protects inefficiency.

Rate-of-Return Regulation – Cost Padding, Not Cost Reductions

- Increases in expenses are fully passed through to customer rates.

- Investment expenditures automatically increase profits, regardless of whether the investment was actually warranted.

- Regulators lack information and knowledge to adequately constrain ROR carriers.

(from FCC's *AT&T Price Cap Order*).

Antidote: Competition and Equal Support Drive Cost Savings to Consumers

- Equal support per line preserves cost advantages/disadvantages that exist in the absence of subsidy payments.
- Equal support per line allows more efficient carrier to undercut less efficient carrier.
- Initially, cost reductions flow to consumer & carrier.
- Carrier prices reveal need for less subsidy to maintain affordable rates.

Competition in Fairbanks – Assuming Deaveraged UNE-Loops (Residential Lines – 2Q 2003)

	ACS-F		GCI		ACS Loop Cost Advantage (Disadvantage)	
	Zone 1	Zone 2	Zone 1	Zone 2	Zone 1	Zone 2
ACS Loop Additional Loop Costs	$16.37* --------	$37.55* --------	$10.65** $12.82	$24.44** $12.82		
Total Loop Costs	$16.37	$37.55	$23.47	$32.26	$7.10	($0.30)
Less ACS Local Rate *Less* SLC	$12.50 $6.00	$12.50 $6.00	$12.50 $6.00	$12.50 $6.00		
Net To Be Recovered Thru Other Rates or USF	($2.13)	$19.05	$4.97	$18.76	**$7.10**	**($0.30)**
Less 2Q 2003 USF	$4.21	$9.47	$4.21	$9.47		
Net To Be Recovered in Other Rates	($6.34)	$9.58	$0.76	$9.29	**$7.10**	**($0.30)**

*ACS Embedded Cost of $29.50 disaggregated proportionately according to weighted average of embedded costs by Zone, as listed in ACS-F Disaggregation Plan (p.4).

**UNE-Loop Rate of $19.19 disaggregated proportionately according to weighted average of embedded costs by Zone, as listed in ACS-F Disaggregation Plan (p.4).

Bad Medicine: USF Based on CETC Costs

- Eliminates incentives for the CETC to be more efficient than the ILEC (*i.e.*, CETC reduces own USF support by reducing its costs).

- CETC has same incentives as ILEC to increase costs to increase revenues.

- Limiting ILEC and CETC USF payments would require intensive regulation.